

**SUPPORTING STATEMENT**  
**for the Paperwork Reduction Act Information Collection Submission for**  
***Form Custody***

**A. JUSTIFICATION**

**1. Necessity of Information Collection**

Section 17(a)(1) of the Securities Exchange Act of 1934 (“Exchange Act”) provides that broker-dealers must make and keep records, furnish copies of the records, and make and disseminate reports as the Securities and Exchange Commission (“Commission”), by rule, prescribes.

The Commission has adopted Rule 17a-5 (17 CFR 240.17a-5) under the Exchange Act, which is one of the primary financial and operational reporting rules for broker-dealers.<sup>1</sup> Rule 17a-5(a) requires broker-dealers to file Form X-17A-5 (17 CFR 249.617), the Financial and Operational Combined Uniform Single Report (“FOCUS Report”). Rule 17a-5(a) also requires broker-dealers that compute certain net capital charges in accordance with Appendix E to Rule 15c3-1 (17 CFR 240.15c3-1e) to file certain additional reports.

On July 30, 2013, the Commission adopted amendments to Rule 17a-5,<sup>2</sup> which, among other things, require a broker-dealer to file new Form Custody (17 CFR 249.639) with its designated examining authority (“DEA”) within 17 business days after the end of each calendar quarter and within 17 business days after the date selected for the broker-dealer’s annual report if that date is not the end of a calendar quarter. Form Custody is designed to elicit information about whether a broker-dealer maintains custody of customer and non-customer assets, and, if so, how such assets are maintained.

**2. Purpose and Use of the Information Collection**

The purpose of Form Custody is to provide information about the custodial activities of broker-dealers that can serve as a starting point for securities regulators to undertake more in-depth reviews of these activities as they deem appropriate.

**3. Consideration Given to Information Technology**

Form Custody would generally be filed electronically with the broker-dealer’s DEA.

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<sup>1</sup> Rule 17a-5 is subject to a separate Paperwork Reduction Act (“PRA”) filing (Office of Management and Budget (“OMB”) Control Number 3235-0123).

<sup>2</sup> See Broker-Dealer Reports, Exchange Act Release No. 70073 (July 30, 2013), 78 FR 51910 (Aug. 21, 2013).

#### **4. Duplication**

The Commission is aware that some overlap exists between the information collected from investment advisers on Form ADV and the information that would be collected from broker-dealers dually-registered as investment advisers in Item 8 of Form Custody. However, these two forms also contain a significant amount of non-overlapping material, reflecting their different purposes and uses. Form Custody is intended to be a single source of readily-available information to assist Commission and DEA examiners in preparing for and performing focused custody exams, and it is particularly important that such information be readily available in the case of dually-registered firms.

#### **5. Effect on Small Entities**

The Commission believes that the burden associated with Form Custody would generally be less for smaller broker-dealers because a broker-dealer that does not clear transactions or carry customer accounts would generally not need to enter detailed information on the form. Of the 513 firms that maintain custody of customer funds and securities, only 19 are small firms.

#### **6. Consequences of Not Conducting Collection**

If the required reports were not made, it would impair the Commission's and the DEAs' ability to detect fraudulent conduct by investment advisers and broker-dealers, including, among other things, misappropriation or other misuse of customer securities and funds. Further, if the required collections were conducted less frequently, the information in the reports would become outdated.

#### **7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)**

There are no special circumstances. This collection is consistent with the guidelines in 5 CFR 1320.5(d)(2).

#### **8. Consultations Outside the Agency**

The Commission requested comment on the PRA analysis in the proposing release.<sup>3</sup> The Commission received two comments on the PRA analysis of Form Custody.

The Commission received one comment in response to Item 8 of Form Custody, as proposed, noting that the information sought in Item 8 was largely the same as information collected from investment advisers on Form ADV.<sup>4</sup> As noted above, the Commission is aware that some overlap exists between the information collected from investment advisers on Form ADV

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<sup>3</sup> See Broker-Dealer Reports, Exchange Act Release No. 64676 (June 15, 2011), 76 FR 37572 (June 27, 2011).

<sup>4</sup> See letter from James J. Angel, Associate Professor of Finance, Georgetown University, to the Securities and Exchange Commission (Aug. 26, 2011), available at <http://www.sec.gov/comments/s7-23-11/s72311-17.pdf>.

and the information that would be collected from broker-dealers dually-registered as investment advisers in Item 8 of proposed Form Custody. However, these two forms also contain a significant amount of non-overlapping material, reflecting their different purposes and uses. Form Custody is intended to be a single source of readily-available information to assist Commission and DEA examiners in preparing for and performing focused custody exams, and it is particularly important that such information be readily available in the case of dually-registered firms. Consequently, the Commission believes that the PRA burden for Form Custody is reasonable in light of its intended purpose. Additionally, the commenter did not indicate disagreement with the hour burden estimate as proposed. Therefore, the Commission is retaining the hour burden estimate without revision.

The second commenter stated that the estimated costs of Form Custody to the industry of \$69,179,670 is “staggering,” and that such costs would likely indirectly be passed on to customers.<sup>5</sup> The commenter did not disagree with the PRA estimate in the proposing release; rather, the commenter focused on the size of the total estimated costs. The Commission recognizes that the requirement to file Form Custody will increase compliance costs for broker-dealers and, consequently, the PRA estimates reflect these costs. The PRA hour burden estimates (and associated internal burden costs), however, are averages across all broker-dealers. The costs incurred by a broker-dealer to comply with the requirement to file Form Custody will depend on its size and the complexity of its business activities. Because the size and complexity of broker-dealers varies significantly, the Commission provided estimates of the average cost per broker-dealer across all broker-dealers.

For these reasons, the Commission believes the PRA burden estimates are reasonable.

#### **9. Payment or Gift**

No payments or gifts were provided to respondents.

#### **10. Confidentiality**

Pursuant to Rule 17a-5(a)(3), Form Custody would be deemed to be confidential.

#### **11. Sensitive Questions**

Not applicable. No inquiries of a sensitive nature are made. No Personally Identifiable Information (PII) is collected.

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<sup>5</sup> See letter from Howard Spindel and Cassandra Joseph, Integrated Management Solutions USA LLC, to the Securities and Exchange Commission (Aug. 26, 2011), available at <http://www.sec.gov/comments/s7-23-11/s72311-20.pdf>. The cost of \$69,179,670 was reflected in the Economic Analysis in the proposing release. See Broker-Dealer Reports, 76 FR at 37601.

## **12. Burden of Information Collection**

As noted above, all registered broker-dealers would be required to file Form Custody with their DEAs once each calendar quarter. As of December 31, 2011, there were 4,709 registered broker-dealers. Based on staff experience, the Commission estimates that, on average, it would take a broker-dealer approximately 12 hours to complete Form Custody, for an annual disclosure burden of approximately 226,032 hours.<sup>6</sup>

## **13. Costs to Respondents**

Form Custody does not impose any costs other than internal labor costs that are associated with the hour burden described in Item 12 above.

## **14. Costs to Federal Government**

There are no costs to the Federal Government associated with Form Custody.

## **15. Changes in Burden**

Not applicable. This is a new collection of information.

## **16. Information Collection Planned for Statistical Purposes**

Not applicable. The information collected is not used for statistical purposes.

## **17. Approval to Omit OMB Expiration**

The Commission is not seeking approval to omit the OMB expiration date.

## **18. Exceptions to Certification for PRA Submissions**

This collection complies with the requirements in 5 CFR 1320.9.

## **B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

This collection does not involve statistical methods.

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<sup>6</sup> 4,709 brokers-dealers x 4 times per year x 12 hours = 226,032 hours.